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IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

UNITED STATES OF AMERICA,
Petitioner,
v.
JOHN O. IRVINE AND FIRST TRUST NATIONAL ASSOCIATION,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF *AMICUS CURIAE* OF JOHN G. ORDWAY, JR. AND MARGARET M. ORDWAY IN SUPPORT OF RESPONDENTS

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BRIEF *AMICUS CURIAE* OF JOHN G. ORDWAY, JR. AND MARGARET M. ORDWAY IN SUPPORT OF RESPONDENTS

STATEMENT OF INTEREST

John G. Ordway, Jr. is the brother of the late Sally Ordway Irvine, for whom Respondents are the personal representatives. Mr. Ordway also was the beneficiary of a trust established in 1917 by their grandfather, Lucius P. Ordway. Like Mrs. Irvine, upon the death of the trust's last surviving income beneficiary in 1979, Mr. Ordway validly disclaimed a portion of his interest in the trust corpus in accordance with state law. On their gift tax returns for the appropriate periods, Mrs. Irvine

and Mr. Ordway each took the position that their disclaimers were not subject to federal gift tax because 1) the disclaimers were valid under state law, and 2) federal regulations imposing a gift tax on otherwise valid disclaimers could not be applied where the interest disclaimed had been created by a transfer in trust made prior to enactment of the Gift Tax Act in 1932 (Revenue Act of 1932, ch. 209, 47 Stat. 169 (1932)). Petitioner United States of America, acting through the Internal Revenue Service, disagreed, and litigation ensued.[1]

After the Ordways prevailed in the district court, a divided panel of the United States Court of Appeals for the Eleventh Circuit reversed, holding that the disclaimer was subject to federal gift tax. *See Ordway v. United States*, 908 F.2d 890 (11th Cir. 1990), *cert. denied*, 111 S. Ct. 2916 (1991). The facts in the *Ordway* and *Irvine* cases are "virtually identical" (Pet. App. 17a).

The *Ordway* case, on remand from the Eleventh Circuit, remains pending in the United States District Court for the Southern District of Florida for the resolution of certain disputed valuation issues. *See Ordway v. United States*, No. 87-8187 (S.D. Fla.). As such, it would be governed by a decision of this Court in the *Irvine* case. *See Harper v. Virginia Dep't of Taxation*, 61 U.S.L.W. 4664 (U.S. June 18, 1993). Mr. and Mrs. Ordway thus have a direct and substantial interest in this Court's disposition of the case on the merits.

Consent to the filing of this brief has been given by petitioner and respondents, and is filed herewith.

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[1] Margaret M. Ordway, Mr. Ordway's wife, consented to being deemed to have made one-half of the alleged gifts attendant to her husband's 1979 disclaimer and thus was a party in the litigation to recover the tax assessed and paid. *See* 26 U.S.C. § 2513.

SUMMARY OF ARGUMENT

I.

For federal gift tax purposes, the disclaimer of an interest created in a 1917 transfer into trust cannot be subjected retroactively to rules implementing the 1932 Gift Tax Act. Section 501(b) of that Act expressly prohibits the retroactive taxation of gifts. The imposition of tax based upon new rules added after the irrevocable transfer which created the interest, and the disclaimer right associated therewith, violates this statutory nonretroactivity. The rule to be applied is simple, consistent, and equitable: disclaimers are subject to taxation only under the rules that exist at the time of the transfer creating the interest and its attendant right to disclaim. This principle follows the reasoning of the Court in *Jewett v. Commissioner,* 455 U.S. 305 (1982), which found no violation of Section 501(b) of the Gift Tax Act for the stated reason that the disclaimer subject to tax involved an interest whose creation postdated the statute. In all other respects *Jewett,* which construed a Treasury Regulation that is inapplicable to pre-Act interests and that governs only the timeliness of disclaimers, does not bear on the question of retroactivity presented in this case.

Congress made the 1932 Gift Tax Act nonretroactive to protect the settled expectations of donors who, in reliance upon the law then in existence, made irrevocable gifts and parted with their property prior to the Gift Tax Act. The statutory provision was intended to spare such donors from the unintended and unanticipated effects of an entirely new tax which, if applied, could compromise the purposes of their gift and estate planning and lead to the disparate treatment of similarly situated beneficiaries. Donors are thus entitled by statute to know the rules applicable to their irrevocable actions before those actions are taken. In the disclaimer context, these policies require that the statutory protection against retroactive taxation attach when a donor's irrevocable transfer creates

the interest later disclaimed. A disclaimer is the formal refusal to accept a gift, which, if made in accordance with applicable state law, allows property to pass from the original settlor as if the person disclaiming did not survive to accept and receive the gift. Instead, the property passes to an alternate recipient selected by the settlor, in accordance with the settlor's irrevocable instructions. These are the interests within Congress's concern in 1932, and every one of them would be sacrificed if, as the Government urges, changes in rules governing gift taxation are made applicable only with regard to the date of the disclaimer.

This proper rule of construction is supported by abundant and uniform precedent, and the plain language of the Government's own regulations. In the years following 1932, Congress has acted to change the gift tax laws specifically applicable to disclaimers and related powers four times, most recently in 1981. In every case it has maintained the principle of nonretroactivity, applying changes only to disclaimers of interests and related powers created after passage of the new legislation. This unbroken line of congressional precedent builds on the original nonretroactivity of the gift tax. Together they establish the principle that retroactivity can only be determined with reference to the date on which a disclaimed interest is created. In other words, the rules governing the taxability of a disclaimer are those that exist at the time the interest disclaimed is created.

The Government cites no precedent to the contrary. *Jewett v. Commissioner* held that a contingent remainder interest was a property right which, if deemed under a federal timeliness standard to have been accepted, could be taxed upon subsequent disclaimer. That case did not hold that a disclaimer was the relevant "transfer" for purposes of determining retroactivity; it could not so hold, as it involved a 1939—post-Act—transfer into trust. Other examples offered by the Government in which property interests created prior to 1932 could be taxable

upon transfer similarly are inapposite. None, for example, involves the exercise of a disclaimer or a related power. Rather, they involved gifts already reduced to ownership and possession, in which case the donor no longer retained an interest, or transactions that were subject to alteration after passage of the taxing statute.

II.

The statute's limitation to disclaimers of interests created after June 6, 1932 is also evident in implementing regulations (Treas. Reg. § 25.2511-1(c)) which consider potentially taxable only disclaimers of interests created in "taxable transfers." That phrase, which has appeared in the relevant Treasury Regulation since 1958, is defined by statute to include only transfers occurring after passage of the Gift Tax Act. It therefore does not embrace the Ordway Trust and the Irvine disclaimer is not taxable.

The Government is wrong as a matter of history and law that § 25.2511-1(c)(2) is merely a "safe harbor" whose inapplicability—for any reason—results in a finding of taxation. The general understanding shared by taxpayers and the Service alike after 1932 was that disclaimers valid under state law were not "transfers," and therefore not within the scope of the gift tax. There is no question that the regulation was intended to add an *additional* trigger for taxation, deeming an interest to have been accepted even if still subject to disclaimer under state law. This Court's conclusion in *Jewett* that a federal timeliness standard was consistent with the statute is not to the contrary.

Section 25.2511-1(c)(2) similarly can provide no basis for any claim that Mrs. Irvine's—but not John Ordway's—constitutional rights would be violated by the imposition of taxation. The constitutional claim depends in the first instance upon a construction of the regulation's retroactivity that is inconsistent with the regulation's plain language and effective date.

ARGUMENT

I. TAXATION OF THE IRVINE DISCLAIMER IS PRECLUDED BY THE STATUTORY NONRETROACTIVITY OF THE 1932 GIFT TAX ACT

A. This Case Involves Only The Applicability Of The Gift Tax Act's Retroactivity Provision, Not The Scope Of The Tax

Unlike *Jewett v. Commissioner*, 455 U.S. 305 (1982), this case presents no issue as to the scope of the gift tax under 26 U.S.C. §§ 2501(a) and 2511(a). Rather, the question presented in this case is whether rules promulgated pursuant to the 1932 Gift Tax Act for the taxation of disclaimers apply to a disclaimer of an interest created fifteen years prior to enactment of the tax through a 1917 transfer into trust. Construction of the 1932 Act must begin, of course, with a review of the statutory language. *See, e.g., Commissioner v. Soliman*, 113 S. Ct. 701, 704 (1993). The only statutory language relevant here is that which makes imposition of the gift tax purely prospective: "The tax shall not apply to a transfer made on or before the date of enactment of this Act [June 6, 1932]." Revenue Act of 1932, ch. 209, § 501(b), 47 Stat. 169, 245. This language embraces the exercise of a disclaimer power over an interest created in a pre-Act transfer, and as a consequence no additional federal standard can be applied to determine the taxability of the Irvine disclaimer. Because the disclaimer at issue here satisfied all state law requirements in existence when the interest was created, it is not subject to tax and the decision of the court of appeals must be affirmed.

This Court in *Jewett*, consistent with the view that Congress intended the gift tax to reach a wide range of direct and indirect transfers, found that the disclaimer of an interest created in 1939 could be taxed. *See* 455 U.S. at 309-10. The Government presents *Jewett* as con-

trolling, and argues that the broad policy of the gift tax to complement the estate tax scheme requires that the Irvine disclaimer be taxable. Pet. Br. 14-16, 18. Both *Jewett* and the policy-driven expansiveness of the gift tax are not relevant here, however, and appeals to them are misguided. The question is not what sorts of property interests may be subject to the Act upon transfer, but *which* transfers otherwise within the scope of the tax were specifically exempted from federal rules of taxation by Congress through the nonretroactivity provision of § 501(b) of the Act. To answer that question, it is necessary to review an entirely different set of precedents and policy considerations, none of which are discussed in the Government's brief.

B. The Retroactivity Of The Irvine Disclaimer For Gift Tax Purposes Must Be Judged With Reference To The Creation Of The Ordway Trust In 1917, To Which The Disclaimer Relates Back

The Government contends categorically that the 1979 Irvine disclaimer is the only event relevant to determining whether or not taxation of that disclaimer is impermissibly retroactive. Pet. Br. 17-20. This is wrong; for purposes of *retroactivity* the only date having significance is 1917, when the Ordway Trust was created, when Lucius Ordway irrevocably gave his grandchildren an interest then subject to valid disclaimer under state law without penalty, and when Mr. Ordway specified who would take in the event a grandchild exercised his or her state-law disclaimer rights or died. The 1932 Act provided for nonretroactive application to protect settled expectations such as these, formed years earlier through irrevocable gifts into trust. To understand why the nonretroactivity provision may only be construed in this manner it is necessary to review the operation of the disclaimer power, examine the purposes of the provision as expressed by Congress, and explore an unbroken line of legislative enactments carrying forward the 1932 concept of retro-

activity specifically in the context of disclaimers and related powers.

It is appropriate to begin with an explanation of the disclaimer power. A disclaimer is the formal refusal to accept a gift; it is a creature of state law, and acts under state law to cause an *inter vivos* or testamentary transfer to pass as if the disclaimant did not survive to accept and receive the gift. *See, e.g.*, Minn. Stat. Ann. §§ 525.-211, 525.532 (West 1988). A disclaimer thus is unlike an ordinary passing of property, in which a donor voluntarily parts with property which he or she owns and possesses. Rather, it is the exercise of the formal power to refuse or reject a gift *ab initio*, the consequence of which is the passage of the interest from the original settlor to an alternate recipient selected *by the settlor*, in accordance with the *settlor's* irrevocable instructions. A disclaimer thus relates back to the date of the original transfer that created the interest disclaimed. *Stoehr v. Miller*, 296 F. 414, 425 (2d Cir. 1923) (1922 disclaimer related back to 1917 transfer into trust to defeat seizure of trust assets under subsequently enacted Trading With the Enemy Act); *cf. United States v. Merchants Nat'l Bank of Mobile, Ex'r.*, 261 F.2d 570, 575 (5th Cir. 1958). Its effect "is to put [the person disclaiming] in the same position as though the beneficial interest had never vested in him, his disclaimer operating retroactively." Austin W. Scott and William F. Fratcher, *The Law of Trusts*, § 36.1 at 391-92 (4th ed. 1987). For gift tax purposes this is critical, because a distribution to a beneficiary from trust is not deemed to be a gift when *distributed*, but rather when the original property was irrevocably placed into trust—here, in 1917. 26 U.S.C. §§ 2511 and 2501(a)(1).[2]

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[2] With the generation-skipping transfer tax, Congress has chosen to tax certain beneficiaries upon changes in or distributions of their interests in trusts. *See* 26 U.S.C. §§ 2611(a) and 2612. In keeping with the general rule, this tax was applied prospectively,

A disclaimer thus relates back to the date when the underlying interest was created, not when the disclaimer power is subsequently exercised. And indeed, in passing legislation affecting the taxability of disclaimers, Congress has implemented precisely this understanding. On every such occasion Congress has changed the gift tax laws prospectively only, and has defined prospectivity in terms of the date of the transfer creating the interest disclaimed, not the date of the subsequent disclaimer of that interest. In 1976, for example, Congress added Section 2518 to the Internal Revenue Code ("Code"), which was intended to make more uniform the federal taxation of disclaimers. Section 2518 subjects to gift tax any disclaimer, *inter alia*, made more than nine months from the "transfer creating the interest," even if the disclaimer still is valid under state law. Tax Reform Act of 1976, Pub. L. No. 94-455, § 2009(b), 90 Stat. 1893. Section 2518 was made effective prospectively, "with respect to transfers creating an interest in the person disclaiming made after December 31, 1976." Prospective application of the change in the law, in other words, turned not on the *date of the disclaimer* but on the *date of creation of the interest disclaimed*.[3] Congress amended Section 2518 in 1981, to minimize further the variation in the taxability of disclaimers that resulted from differences in state law. And again, the changes were applicable only to the disclaimers of interests created in *transfers* occurring after the legislation.[4] *See* Eco-

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to applicable changes in and distributions of interests only for *trusts created after* the effective date of the legislation. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, § 1433(b)(1) and (2), 100 Stat. 2731.

[3] In *Jewett*, this Court characterized the 1976 amendment's formulation as reflecting "the legislative decision not to apply [the new] standards retroactively." 455 U.S. at 317.

[4] Treasury regulations interpreting these statutory provisions incorporated the same definition of retroactivity. *See* Treas. Reg. § 25.2518-1(c).

nomic Recovery Act of 1981, Pub. L. No. 97-34, § 426(b), 95 Stat. 318. Thus, for purposes of gift taxation, Congress through successive prospective enactments in 1932, 1976, and 1981 has divided all disclaimers into four groups, based upon the date of creation of the interest disclaimed: interests created prior to June 7, 1932, interests created between June 7, 1932 and December 31, 1976, interests created between January 1, 1977 and December 31, 1981, and interests created on or after January 1, 1982. The continuity and predictability of disclaimer taxation so viewed—from the standpoint of the donor, the recipient, and the Treasury—would be lost under the rule urged by the Government. *Cf. Commissioner v. Lester*, 366 U.S. 299, 304 (1961) ("[a]s we have frequently stated, the Code must be given as great an internal symmetry and consistency as its words permit") (internal quotations omitted).

The same policies underlying the nonretroactivity of congressional legislation dealing with disclaimers is also evident in 1942 legislation making taxable the exercise and the release of general powers of appointment.[5] The release of a general power is like a disclaimer because in each instance the holder, by the act of releasing or disclaiming, foregoes the right to receive property designated for him or her, allowing the property to pass pursuant to the instructions provided by the original settlor. Indeed, the Court in *Jewett v. Commissioner* analogized the two. *See* 455 U.S. at 317-18. The tax established by the 1942 legislation was imposed prospectively, not with respect to when a power was exercised or released, but when it was *created*. *See* Revenue Act of 1942, Pub. L. 77-753, § 403(d), 56 Stat. 798. For interests created before passage of the legislation, holders were free for a period to release their powers without penalty. Congress

[5] A general power of appointment permits the holder, upon exercise, to designate the recipient of an interest—including the designation of himself or herself. 26 U.S.C. § 2514(c).

amended the provision in 1951, to eliminate entirely any taxation of pre-42 powers so long as they were released in accordance with state law. This was done with the express recognition that many powers had been created prior to 1942 in reliance on the prior law, and that forcing holders to release within the grace period or be taxed (or simply to be taxed upon tardy release through lack of knowledge of the new law), "would seriously impair the arrangements made by the creator of the power for the benefit and protection of his family." S. Rep. No. 382, 82d Cong., 1st Sess. (1951), *reprinted in* 1951 U.S.C.C.A.N. 1530, 1531. Again, in the 1951 legislation Congress respected the principle of nonretroactivity, and achieved its goals of repose by defining retroactivity with reference to when an interest was created, not when it was released. *See* 26 U.S.C. § 2514(a) and (b).

Protecting the legitimate expectations of donors who had irrevocably parted with their property indeed is the fundamental policy behind the nonretroactivity provision of the 1932 Gift Tax Act, and the subsequent legislative actions built consistently on the policies first there protected. Passage of the 1932 Act, of course, followed decisions of this Court that had struck down as unconstitutional prior gift tax statutes having a retroactive component. *See Untermyer v. Anderson*, 276 U.S. 440 (1928); *Nichols v. Coolidge*, 274 U.S. 531 (1927); *cf. Blodgett v. Holden*, 275 U.S. 142 (1927), *modified*, 276 U.S. 594 (1928). *See also* Pet. Br. 16 n.5. As the pertinent legislative materials make clear, the 1932 legislation was passed to comport with these decisions, and to codify what this Court, in 1932, deemed to be the constitutional limitations on the power to impose an excise tax: "The gift tax may not constitutionally apply to gifts made prior to the date of the enactment of the act imposing the tax." S. Rep. No. 665, 72d Cong., 1st Sess., at 43 (1932); *accord*, H.R. Rep. No. 708, 72d Cong., 1st Sess., at 31 (1932). *See also* Pet. Br. 16 n.5.

In both the judicial and the complementary legislative actions, retroactivity was proscribed to secure what was considered to be fundamental fairness to settlors. As a contemporary commentator observed: "[I]f these decisions can be harmonized by a single doctrine it would probably be as follows: Retroactive application of a tax law is permitted only where it would not operate unfairly by attaching consequences to an act by a taxpayer which he could not reasonably have been foreseen." Ralph R. Neuhoff, *Retrospective Tax Laws*, 21 St. Louis L. Rev. 1, 2 (1935). *See also Welch v. Henry*, 305 U.S. 134, 147 (1938). Thus, in determining how to apply to disclaimers the 1932 Gift Tax Act's requirement of nonretroactivity, the touchstone is protection of the settlor's reasonable expectations.[6] *Cf. Cottage Savings Ass'n v. Commissioner*, 111 S. Ct. 1503, 1508-09 (1991) (reviewing cases from the 1920s to determine the meaning of a statute that codified their holdings). And to accomplish this goal, nonretroactivity requires that the gift tax consequences of a disclaimer be judged with reference to the rules in effect when the irrevocable transfer into trust was made.

Lucius Ordway's decision in 1917 to establish a trust and structure it as he did was shaped by the law as it then existed. He could not know that fifteen years

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[6] Enforcement of the nonretroactivity provision to protect a donor's reasonable expectations involves consideration of congressional intent, not the enforcement of the donor's constitutional rights. Such latter inquiry, of course, would be appropriate to the extent such rights bear upon the beneficiaries' rights. *See Hodel v. Irving*, 481 U.S. 704, 711-12 (1987). And in this regard it bears noting that, while *Untermyer* has not been extended beyond the 1932 Gift Tax Act—which is at issue here—its validity in that context has not been undermined. *See United States v. Hemme* 476 U.S. 558, 567-68 (1986); *United States v. Darusmont*, 449 U.S. 292, 299 (1981); *Ferman v. United States*, 993 F.2d 485, 490 n.7 (5th Cir. 1993).

later Congress would create "a wholly new tax," *United States v. Hemme*, 476 U.S. 558, 568 (1986), and in the view of the Government expose his designated beneficiaries to a financial penalty for taking actions (*e.g.*, refusing to accept a gift through the exercise of a disclaimer power in accordance with state law) or refraining from taking actions which then had no consequences. Had he known, the disclaimer power he gave to his grandchildren could have been replaced, for example, with a general power of appointment, which could have been released without tax consequences.[7] *See* pp. 10-11, *supra*. This potential unfairness arises only with the rule advanced by the Government, which would tax the 1979 disclaimer of a 1917 interest by 1979 standards, yet tax the release of a general power of appointment created at the same time, properly, under the law that existed in 1917. The anomaly of this result is patent: The disclaimer of an interest is taxable, yet the release of the much greater right to cause a transfer to be made to anyone, is not.[8]

It is important to observe that honoring the Gift Tax Act's nonretroactivity provision does not mean that a subsequent disclaimer is wholly *exempt* from a gift tax. Rather, it means that the right created upon the 1917 transfer may not be subjected to *additional* tax rules

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[7] No argument is being made here that what Lucius Ordway did should be nontaxable because it has the same "economic reality" as creation of a nontaxable general power of appointment. *Cf. Commissioner v. National Alfalfa Dehydrating Milling Co.*, 417 U.S. 134, 148 (1974). Rather, the point merely is that Lucius Ordway's irrevocable plans and legally protected interests were compromised because a wholly new tax was imposed on his actions after-the-fact. *Cf. Welch v. Henry*, 305 U.S. at 147.

[8] Indeed, the holder of a general power of appointment may even be the life income beneficiary of the interest over which he or she holds a power without subjecting a subsequent release to taxation. *See* 26 U.S.C § 2514(a); 26 C.F.R. § 25.2514-2(c).

imposed after-the-fact. Lucius Ordway provided for his beneficiaries to have interests subject to disclaimer, so long as they acted in accordance with the state law. That limitation never disappeared. An attempted disclaimer that did not satisfy state law would not act as a refusal to accept, calling into play the substitute beneficiary selected by the settlor. Rather, it would be a retransfer following acceptance by the beneficiary, and in that transaction the settlor's continuing interest would have expired and he would have no legally protectable expectation. It could, therefore, be subjected to a gift tax consistent with both the statutory and constitutional prohibitions against retroactivity. This indeed is the factual context in which the ineffective attempt to disclaim an interest passing as a matter of law by intestate succession was found taxable in *Hardenbergh v. Commissioner,* 198 F.2d 63 (8th Cir.), *cert. denied,* 344 U.S. 836 (1952).[9]

Against these historically protected interests and direct legislative precedents, the Government cites cases and makes arguments that have nothing to do with the retroactivity of disclaimers. *Jewett v. Commissioner,* which the Government claims to be controlling, to the extent relevant at all can only be read as supporting the nontaxability of the Irvine disclaimer. *Jewett* involved the 1972 disclaimer of an interest created in a 1939 transfer. No issues of statutory retroactivity thus were presented, as the Court observed:

> Petitioner also argues that it is unfair to apply the 1958 Regulation "retroactively" to an interest that had been created previously . . . . The argument . . . is based on an assumption that petitioner had a "right" to renounce the interest without tax consequences that was "taken away" by the 1958 Regu-

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[9] No issues of line-drawing need be addressed as to which expectations of the settlor must be honored. The point is that the nonretroactivity provision simply must be read as applying based upon the date of the transfer creating the interest disclaimed. The appropriate rules of taxation will follow as a consequence.

> lation. Petitioner never had such a right. Indeed, petitioner does not argue that taxation of the disclaimers is inconsistent with the statutory provisions imposing a gift tax, which were enacted long before *petitioner's interest in the trust was created.*

455 U.S. at 317 (emphasis added). In concluding that no issue of statutory retroactivity was presented, the Court looked solely to the date when the *Jewett* interest was created, as we do here.[10]

Jewett similarly cannot stand for the "holding" attributed to it by the Government that the "transfer" for purposes of the 1932 Act's retroactivity provision is the disclaimer alone. Pet. Br. 16. Citing the expansive definition of property within the scope of the gift tax set forth in *Smith v. Shaughnessy*, 318 U.S. 176, 180 (1943), *Jewett* indeed held that a contingent future interest is a type of interest, the gift of which, consistent with the statute, could be subject to a federal standard of deemed acceptance; the Court did not hold that *every* disclaimer is taxable, a question not even remotely presented.[11] And except for the passages quoted above which tie retroactivity to the date of creation of an interest, the case has nothing to say as to how the definition of retroactivity is to be implemented. Indeed, the Court concluded that the term "transfer" is ambiguous, ultimately interpreting its

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[10] The Court then observed that no issues of *regulatory* retroactivity were presented, as the disclaimers were made some fourteen years after the regulation in question was adopted. *Ibid.*

[11] The Government correctly states *Jewett's* limited holding in this regard, reciting that: "[t]he Court squarely rejected" the contention that "*any* valid disclaimer would be exempt and the gift tax would never apply." Pet. Br. 31 (emphasis in original). The fact that the Government had a reasonable rationale of deemed acceptance for taxing certain disclaimers not timely made does not mean that it may tax them all. *Cf. Dickman v. Commissioner*, 465 U.S. 330, 341 (1984) (permissible taxation of interest-free intrafamilial loans does not mean that all acts of intrafamilial generosity are taxable).

use in Treas. Reg. § 25.2511-1(c) to refer to the original transfer into trust for purposes of that regulation's federal timeliness standard. *See* 455 U.S. at 311-12, 318.

None of the other cases cited by the Government even involves a disclaimer or a power remotely resembling one. Two of the cases cited by the Government, *Estate of Sanford v. Commissioner*, 308 U.S. 39 (1939), and *Burnet v. Guggenheim*, 288 U.S. 280 (1933), stand only for the proposition that transfers are not complete for gift tax purposes until irrevocable, with the termination of the donor's retained rights to modify the disposition of trust assets the appropriate event of taxation. *Accord*, Treas. Reg. § 25.2511-2(b). Here, of course, Lucius Ordway's transfer into trust was irrevocable when made in 1917, underscoring the appropriateness of considering that action the operative one for gift tax purposes. What Mrs. Irvine possessed and exercised by her disclaimer was only the power under state law to refuse to accept that gift, in which event the disposition of property proceeded as directed by Lucius Ordway in 1917.

The Government's principal citation to cases is for the proposition that a tax is not retroactive merely because "some" of the "facts and conditions upon which its application depends came into being prior to the enactment of the tax." Pet. Br. 19, quoting *United States v. Jacobs*, 306 U.S. 363, 367 (1939). While this is a correct statement of the law, the cases neither address retroactivity in the context of a disclaimer nor support a finding in this case that taxing Mrs. Irvine's disclaimer would be non-retroactive and therefore permissible. *Jacobs* was an estate tax case involving a tenancy by the entirety in which the *statute* expressly applied to tenancies created by transfers made prior to the statute's passage. *Id.* at 365. No question was presented under the Gift Tax Act, which, of course, expressly proscribes retroactive application to pre-Act transfers. Moreover, of critical significance is that Mrs. Irvine merely exercised a limited right not to

accept a gift, while the fundamentally different right of a survivor to own absolutely, to possess, and to dispose of property as he or she wishes upon the death of a co-tenant was at stake and found to be decisive in *Jacobs*. *Id.* at 367-68. The Court there concluded that the surviving co-tenant's ascension to complete ownership and possession made taxation "valid" as against constitutional attack.[12] *Id.* at 368. An analogous conclusion was reached in *Fernandez v. Wiener*, 326 U.S. 340, 348-350, 355-56 (1945) (estate tax case).[13] This characterization stands in stark contrast to Mrs. Irvine's limited right not to accept a gift.

Jacobs and other cases cited by the Government also are distingiushable on a ground of central relevance to the question of whether a statute acts retroactively. In those cases, the decedent—unlike Lucius Ordway—had an opportunity *after* passage of the taxing legislation to reorder his or her affairs to avoid the tax, and so no element of retroactivity was fairly presented. This feature indeed was the express ground for treating two groups of trusts differently in *Reinecke v. Northern Trust Co.*, 278 U.S. 339 (1929) (estate tax case). *See Jacobs*, 306 U.S. at 369; *Chase Nat'l Bank v. United States*, 278 U.S. 327, 334-345 (1929) (estate tax case).[14] It was not

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[12] The Government, of course, agrees that the statutory nonretroactivity of the Gift Tax Act is different from and stricter than any constitutional limitations. Pet. Br. 16-17 n.5. In the statutory context, moreover, ambiguities must be resolved in favor of prospective application. *Hassett v. Welch*, 303 U.S. 303, 314 (1938).

[13] In *Fernandez*, like other community property cases, the surviving co-tenant's interest was created through the operation of law, not a voluntary transfer. *See* 326 U.S. at 348. The absence of a protectible expectation on the part of the "donor" has been recognized as decisive in other retroactivity cases. *See, e.g., Welch v. Henry*, 305 U.S. 134, 147 (1938).

[14] *Cf. Gladney v. Commissioner*, 745 F.2d 955 (5th Cir. 1984), which upheld application of a 1969 tax on distributions by a private, tax-exempt foundation. Although the foundation was estab-

until death that the right to alter ended, and the relevant "transfer" was complete.

The reason why no precedent supports the rule advanced by the Government is that it serves no purpose articulated by Congress in 1932 or thereafter. A rule in which a beneficiary's right to disclaim is taxed based upon the law at the time of the disclaimer upsets the settlor's reasonable expectations, compromises his or her intent, promotes disparate treatment of similarly situated beneficiaries (thereby subverting Congress's purpose in passing 26 U.S.C. § 2518 to assure uniform treatment of beneficiaries), and by the addition of uncertainty frustrates attempts by taxpayers, in the Government's words, "to pursue their important gift and estate planning decisions with certainty." Pet. 21. On the other hand, all of these historically recognized interests in the taxation of gifts are advanced by the simple recognition that retroactivity in the disclaimer context is judged with reference to when the underlying interest was created.

The Government also throws up a straw man of sorts by claiming that respondents can prevail only at the expense of taxing or exempting from tax *every* interest based upon the date of its creation. "Many property rights currently in existence were created before 1932," the Government observes, suggesting that the transfer of none could be taxable if no tax is laid on the Irvine disclaimer. Pet. Br. 17. This simplistic assertion summarily ignores the distinction between gifts that have not been accepted and are subject to disclaimer and those that have been accepted and reduced to ownership and possession.[15] In the former case, as shown above, the donor

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lished as a testamentary trust in 1905, it did not seek tax-exempt status—and become potentially subject to the tax—until 1970. No retroactivity was present as the tax was based upon the trust's decision after passage of the taxing act to take advantage of the benefits of the Code.

[15] In the district court, the Ordways and the Government stipulated that *amicus* John Ordway never accepted "any interest what-

has a protected interest to see his or her irrevocable decisions to their completion. In the latter case, the donor's continuing legal interests have expired.[16]

At the *certiorari* stage, the Government complained that "the decision in this case offers significant new opportunities for gift and estate tax avoidance by members of the wealthiest class of taxpayers." Pet. 21. No "new" opportunities are at stake, however, as the Government itself does not appear regularly—if indeed *ever*—previously to have claimed a gift tax under the 1932 Act on the valid disclaimer of a pre-Act interest. *See* pp. 24-25, *infra; cf. Fuller v. Commissioner*, 37 T.C. 147 (1961) (disclaimer of pre-Act interest taxable where income from interest disclaimed had been accepted; retroactivity issue not addressed). More fundamentally, the idea that nonretroactive taxation operates as a device for evasion does disrespect to congressional intent. Dissenting in *Untermyer v. Anderson*, Justice Brandeis observed that nonretroactivity permits "evasion of the gift tax" by "the vigilant and ingenious." 276 U.S. at 450-51. Yet precisely that result is what Congress prescribed in § 501(b) of the Act, and has reintroduced into the law without exception in subsequent legislation affecting disclaimers and related rights.[17] To the extent Congress was free

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soever" in the portion of the trust he disclaimed. *Ordway v. United States*, No. 87-8187 (S.D. Fla.) (Pretrial Stipulation ¶ 5(f)).

[16] The distinction indeed is present in the 1958 Treasury Regulation which first imposed a separate federal standard for the taxation of disclaimers and which taxed any disclaimer not exercised "within a reasonable time." *See* 26 C.F.R. § 25.2511-1(c) (1958). As a leading contemporary commentator observed, this timeliness rule creates a "presumption of acceptance of the property," following which an otherwise valid disclaimer would be deemed to be a gift. *See* 5 Jacob Mertens, *The Law of Federal Gift and Estate Taxation* § 34.14 at 74 (1959).

[17] Congress elsewhere has elected to enact gift taxes prospectively, sacrificing many, many times the revenue at issue in this case. In

constitutionally to impose a retroactive tax it certainly can be said to have foregone potential revenue; what it preserved in the process, however, was its compact with the American people that, in the gift tax context, settled expectations would be honored and irrevocable actions would not be penalized after-the-fact.

II. DISCLAIMERS OF PRE-ACT INTERESTS ARE NOT WITHIN THE SCOPE OF TREAS. REG. § 25.2511-1(c)(2), AND ARE NOT OTHERWISE TAXABLE UNDER THE GIFT TAX ACT

The Government addresses at length whether the Irvine disclaimer is the disclaimer of an interest arising out of a "taxable transfer," and thus falls within the scope of the disclaimer regulation, 26 C.F.R. § 25.2511-1(c) (1986). To the extent the Gift Tax Act is construed not to apply retroactively to disclaimers of pre-Act interests, of course, the gift tax regulations are inapplicable and no question as to their meaning is presented for resolution. Indeed, it is noteworthy that the regulation itself parallels the non-retroactivity provision of the Gift Tax Act: by its own terms it provides that only disclaimers of post-Act "taxable" transfers may themselves be taxable, and as so interpreted follows the uniform and consistent treatment of adopting rules effective upon the creation of the interest. The Government argues nevertheless that even if the regulation is so limited, disclaimers of pre-Act interests are taxable because *all* disclaimers are taxable unless specifically exempted. Such a reading of the applicable statutes and regulations would be contrary to their plain language and history and would lead to anomalous results.

1986, for example, Congress enacted a generation-skipping transfer tax to replace one first imposed in 1976, but which proved unworkable. *See* Tax Reform Act of 1986, Pub. L. No. 99-514, § 1431 *et seq.*, 100 Stat. 2085, 2717. The revision was made prospective; indeed, irrevocable gifts made in reliance upon the 1976 law were exempted permanently from any tax. *Id.*, § 1433(c), 100 Stat. 2731.

A. "Taxable Transfers" Include Only Those Transfers Occurring After June 6, 1932

The decision of the *en banc* majority of the court of appeals was based upon a reading of § 25.2511-1(c)(2), which addresses the taxability only of disclaimers of interests created in "taxable transfers." Because, as seems self-evident, a nontaxable pre-Act transfer into trust is not "taxable," the court concluded that the regulation was inapplicable and could not serve as a basis for imposing a tax on the Irvine disclaimer. In this regard the plain language of the regulation and associated statutory provisions leave no room for doubt. The term "taxable transfers" is a term of art defined by statute as follows:

> (26 U.S.C.) § 2501. Imposition of tax.
>
> (a) Taxable transfers.—
>
> (1) General rule.—A tax, computed as provided in section 2502, is hereby imposed for each calendar year on the transfer of property by gift *during such calendar year* by any individual, resident or nonresident.

(Emphasis added).[18] As the italicized language (omitted from the statute as reproduced at Pet. 60a) indicates, taxable transfers thus include only those transfers made during calendar years for which a tax may be computed, in accordance with Section 2502. As is apparent, Section 2502 is drafted specifically to exclude any period prior to June 7, 1932. *See* Addendum, *infra*, 1a. Applicable Treasury Regulations also are in accord. The first two sentences of § 25.2511-1(a) (promulgated in 1958), unambiguously equate a "taxable transfer" with a transfer to which the gift tax applies. *See* Addendum, *infra*, 2a.

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[18] Section 2501(a) was added to the Code in 1954. Act of August 16, 1954, c. 736, 68 Stat. 403. The title "[t]axable transfers" was added in 1966 following amendments not relevant here. Foreign Investors Tax Act of 1966, Pub. L. 89-809, § 109(a), 80 Stat. 1575.

The Government thus also is incorrect when it suggests that "taxable transfer" was only added to the regulation in 1986. Pet. Br. 24-25 n.12.

The Government's arguments to the contrary are based upon a selective inattention to relevant regulatory language. Thus, the Government seeks to equate "taxable transfer" with a "completed gift," which concededly occurred in 1917 when Lucius Ordway made an irrevocable transfer into trust. Pet. Br. 24-26. *First,* the regulation relied upon by the Government by its own terms does not apply to disclaimers of interests created prior to January 1, 1977. *See* Treas. Reg. § 25.2518-1(a). *Second,* the regulation equates "taxable transfer" with a "completed gift *for Federal gift tax purposes.*" *Id.* This limitation anchors "taxable transfer" firmly in the language of 26 U.S.C. § 2501 and the 1932 Act, and in rules that define a "completed gift for Federal gift tax purposes" to include only those subject to the gift tax. *See also* Treas. Reg. § 25.2511-2(a) and (b). Since, as all parties agree, the 1917 transfer is not subject to the gift tax, it cannot be a "completed gift for Federal gift tax purposes." Any other conclusion would permit the Gift Tax Act's requirement of nonretroactivity to be overruled by an administrative regulation. *Cf. National Muffler Dealers Ass'n v. United States,* 440 U.S. 472, 477 (1979); *Ernst & Ernst v. Hochfelder,* 425 U.S. 185, 213-14 (1976).

The Government seeks to support its interpretation of the Treasury Regulations by staking a claim to deference because its interpretation of "taxable transfer" has been consistently maintained. Pet. Br. 27. No deference is due an agency's construction of a regulation that is contrary to the regulation's plain meaning, however. *See Gardebring v. Commissioner,* 485 U.S. 415, 430 (1988). Moreover, no authority is cited for this assertion of consistency. The contrary definition appearing in 26 U.S.C. § 2501(a) (added in 1966) and Treas. Reg.

§ 25.2511-1(a) (1958) would in any event belie the claim.

B. Treas. Reg. § 25.2511-1(c)(2) Is Not A "Safe Harbor" From A Rule Of Universal Taxation Of All Disclaimers

The Government contends that, even if it is wrong in construing § 25.2511-1(c)(2) to apply to the disclaimer of a pre-Act 1917 interest, the disclaimer must nevertheless be taxable under the general principle that any gift not specifically exempted from the taxing statute is within it. Pet. Br. 23-27. Thus, the Government argues, § 25.2511-1(c)(2) is merely a "safe harbor" in a sea of taxation, without whose protection the expansive language of the taxing authority would apply automatically. To conclude this is so, however, would require adoption of an irrational and baseless interpertation of the regulation that is at odds with all available historical evidence.[19]

Under the Government's alternative reading, the regulatory "safe harbor" would only *commence* for interests created after June 6, 1932. Thus, for interests in trust created on June 5, 1932, *every* disclaimer would be taxable, even if valid under state law and made within a "reasonable time." A disclaimer made on the same day but stemming from an interest in trust created on June 7, 1932, however, would not be deemed a gift. This result,

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[19] The Government's assertion that it may, by regulation, create a substantive exemption from what it repeatedly characterizes as an unambiguous and unqualified statutory mandate to tax is itself a novel concept. If, as the Government asserts, there is no question but that every disclaimer is within the scope of the gift tax, Pet. Br. 14-16, 27-28, it is not for the agency to say differently. *See, e.g., National Muffler Dealers Ass'n v. United States*, 440 U.S. 472, 477 (1979). The statute, of course, has not been read so broadly, as discussed *infra*. The Court in *Jewett v. United States* did consider the taxability of disclaimers, but only to conclude that Treas. Reg. § 25.2511-1(c) was consistent with its statutory authority. *See* 455 U.S. at 309-310.

required according to the Government by a regulation not promulgated until 1958, retroactively penalizes the settlor who established a trust *earlier*, prior to passage of the Gift Tax Act. It also requires the startling and historically repudiated conclusion that the acceptance of a gift is not required for the federal gift tax to be applied, and that a person thus may be forced to accept an unsolicited gift or be taxed upon refusing to do so. *See Jewett*, 455 U.S. at 323 (Blackmun, J., dissenting). The Government's "safe harbor" theory is arbitrary and capricious and indeed implicates a principal factor employed in contemporary analysis of the constitutionality of retroactive taxation. *See United States v. Hemme*, 476 U.S. at 569 (considering "whether, without notice, a statute gives a different and more oppressive legal effect to conduct undertaken before enactment of the statute").

An interpretation that avoids such anomalies and comports with historical evidence is that § 25.2511-1(c) is an effort by the Commissioner, commenced in 1958, to carve out a limited exemption from the prevailing understanding that disclaimers valid under state law were not considered "transfers," and thus were not subject to gift tax at all. Notwithstanding the admitted breadth of the gift tax, prior to 1958 no separate federal standard existed for the taxation of disclaimers. After passage of the 1932 Act, case law, to the extent it existed, was all to the effect that disclaimers that were valid under state law involved gifts that were never accepted, and thus not "transferred" upon exercise of a disclaimer; accordingly, there was no federal standard of deemed acceptance superimposed on state law, and valid disclaimers thus were not subject to gift tax. This Court in *Jewett* so concluded, discussing at length the early cases of *Brown v. Routzahn*, 63 F.2d 914 (6th Cir.), *cert. denied*, 290 U.S. 641 (1933), and *Hardenbergh v. Commissioner*, 198 F.2d 63 (8th Cir.), *cert. denied*, 344 U.S. 836 (1952), and observing that "under those cases state law controlled both the 'right' to renounce and the 'timeliness' of the renunciation" for

federal gift tax purposes. 455 U.S. at 315. *Jewett* acknowledged, in other words, that a disclaimer valid under state law was not subject to gift tax prior to the 1958 regulation. This understanding remained the law through the 1950s,[20] and explains why the issue of retroactive taxation of disclaimers of pre-Act interests was not decided in the years following 1932: *no* valid disclaimers were thought to be taxable.

Against this background, the 1958 regulation's addition of a federal "reasonable time" standard quite clearly was not an effort to exempt disclaimers from taxation. On the contrary, it provided the rationale for *taxing* a disclaimer valid under state law but held long enough to be deemed for tax purposes to have been accepted under a newly adopted federal standard. *See Jewett*, 455 U.S. at 316-17 & n.17; pp. 18-19, *supra*. The 1976 legislation promoted uniformity in the taxation of disclaimers by codifying a "reasonable time" to be nine months, and the 1986 version of Treas. Reg. § 25.2511-1(c)(2) implemented the statutory change for disclaimers of interests created after December 31, 1976. With respect to disclaimers of interests created prior to that date, the "reasonable time" standard remained the same, and there is no evidence that the 1986 revision altered in any way the Service's conception of the regulation as attempting solely to add the

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[20] *Brown v. Routzahn*, holding that a valid disclaimer under state law is not a transfer for federal gift tax purposes, was assumed by "taxpayers and presumably the Bureau of Internal Revenue" as settling the law. *See* Christian Marius Lauritzen, II, *Only God Can Make An Heir*, 48 Northwestern U. L. Rev. 568, 577-78 n.57 (1953), quoting American Bar Ass'n, *Report of Committee on Federal Estate and Gift Taxes*, Recommendation III, p. 19 (1953); Edward T. and Sheila M. Roehner, *Renunciation As Taxable Gift—An Unconstitutional Federal Tax Decision*, 8 Tax L. Rev. 289, 314 (1953). There is no statute of limitations on the failure to file a gift tax return reporting a taxable disclaimer. *See* 26 U.S.C. § 6501(c)(3). One can only speculate how many thousands of unreported disclaimers would become subject to tax, penalties, and interest if the Government's alternative position in this case were upheld.

concept of deemed acceptance through creation of a federal standard.

So understood, the Government's *post-hoc* characterization of the regulation as a "safe harbor" seems hopelessly divorced from any basis in law, fact, or history. It is contrary to the Secretary's clear intent in promulgating the regulation, and is entitled to no deference. *See Gardebring v. Commissioner,* 485 U.S. at 430. The regulation's purpose, by imposing a standard of deemed acceptance of a gift still subject to valid disclaimer, is to prescribe exceptions to the general understanding that such a disclaimer will not be subject to tax. To the extent the regulation—as limited to post-Act "taxable" transfers—is interpreted not to cover every disclaimer theoretically within the scope of the Act, what is omitted remains within the general rule of nontaxability. To construe the Service's own regulation, or the statute, as requiring a contrary result is to rewrite the entire history of the regulation and the Service's interpretation of the Gift Tax Act. It imputes to Congress and the Service a view that all valid disclaimers are taxable—one that is precisely the *opposite* of what was believed when both the statute and the regulation were first written. Thus *Dickman v. Commissioner,* 465 U.S. 330 (1984), which found the Gift Tax Act broadly applicable to transactions found to be transfers, is inapposite because the Service has never so characterized every valid disclaimer. So too is the rule that outright exemptions from the taxing statute are to be narrowly construed, as the regulation is not an exemption.[21]

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[21] The Government's reliance upon principles of narrow construction for exemptions from taxation would in any event be difficult to accept here, even assuming that canon applicable to Treasury Regulations. Section 25.2511-1(c) on its face deals only with *testamentary* transfers, as Judge Loken observed, concurring with *en banc* majority in the court of appeals. Pet. App. 12a-16a. Nevertheless, the principles of the regulation have been extended by the Government to *inter vivos* transfers, merely supporting the argument in the text that the omission from § 25.2511-1(c)(2) of a

C. Treas. Reg. § 25.2511-1(c)(2) Could Not Apply Differently To The Irvine And Ordway Disclaimers

The overriding need for a uniform rule of taxation is made all the more evident by respondents' suggestion at the *certiorari* stage that Mrs. Irvine's disclaimer could not constitutionally be taxed under the 1986 disclaimer regulation, as the Government seeks to construe it. Observing that Mrs. Irvine learned of her right and reached majority prior to 1932, respondents argued in the alternative that the regulatory requirement that she have disclaimed within a "reasonable time" of her knowledge of a right to disclaim could not have been satisfied because it would have expired even before passage of the 1932 Act. No such certainty is possible, however, as "reasonable time" determinations are questions of fact under the regulation. *See Patterson v. Commissioner*, 46 T.C.M. (CCH) 618 (1983). Moreover, respondents' argument is fundamentally flawed because the 1986 regulation, by the Government's reckoning, could not have applied to disclaimers made prior to January 1, 1955. The original 1958 disclaimer regulation construed the 1954 Internal Revenue Code, and by its own terms purports to be retroactive only to January 1, 1955—the effective date of the 1954 act. *See* 23 Fed. Reg. 8904 (1958). The 1986 regulation, which amended the 1958 regulation and was based on 1976 legislation, similarly was not made retroactive to 1932. *See* 51 Fed. Reg. 28366 (1986). Clearly, the 1986 regulation could not require that a disclaimer be made prior to 1932, as respondents speculate that the Government would require.[22] Accordingly, the dates when

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reference to a specific class of disclaimers does not mean they are taxable. *See* 5 Boris I. Bittker and Lawrence Lokken, *Federal Taxation of Income, Estates and Gifts*, ¶ 121.7.1 at 121-47 (2d ed. 1993).

[22] The Government does allege that all disclaimers are taxable, and have been so since 1932. In that event John Ordway, who learned of his interest and reached majority in 1943, would have been denied any chance to disclaim without tax consequences.

Mrs. Irvine learned of her interest and reached the age of majority have no bearing on this case, and do not distinguish her disclaimer from other Ordway Trust disclaimants.[23] Moreover, this speculation as to dates underscores the need for a uniform standard, under which similarly situated taxpayers are treated the same based upon the rules in effect when their interests were created.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

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[23] Statements to the contrary apparently made in error by Government Counsel below cannot, of course, alter the effective date of the regulations. *See* Pet. Opp. 8 n.9.